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Roger J. Vaughan

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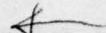
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THE USE OF SUBSIDIES IN THE
PRODUCTION OF CULTURAL SERVICES

Roger J. Vaughan
The Rand Corporation

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I. INTRODUCTION

The purpose of ~~this paper is to explore~~ some basic issues relevant to the use of public funds to support the production and delivery of cultural services, ^{such as} What are the policy goals of federal assistance to the arts? ^{and how} Does the way in which support is provided help in the attainment of these goals? 

These questions may seem rather obvious to those engaged in the business of providing for local cultural needs. The necessity of public support is taken for granted. When reasons are advanced, they tend to be couched in vague terms. For example, the purpose of the National Endowment for the Arts (NEA) was described, at its inception, as:

To make the arts more widely available to millions of Americans, to preserve our cultural heritage for present and future generations, to strengthen cultural organizations and to encourage the creative development of the nation's finest talent.

The volume of federal support for cultural activities is by no means small. The NEA will fund nearly \$80 million worth of cultural activities in this fiscal year, and the IRS will allow individual businesses to avoid nearly \$200 million in taxes through contributions to non-profit cultural institutions. States will contribute nearly \$60 million. Yet, if this seed money from the public is to be used effectively, we must ensure that the manner in which it is distributed encourages the attainment of desired goals.

There is considerable confusion over goals and the way in which money is made available for cultural activities does not appear to be consistent with these goals. This paper may be read as an outline for areas of future research. However, it is addressed primarily to those charged with determining the distribution of public funds for the support of the arts, and is intended to question some of the basic principles upon which allocations are traditionally made.

The arts face a severe financial crisis, exacerbated by the present economic recession. Economic and business administration techniques are rarely applied to the running of arts institutions--indeed, it appears as if they are often deliberately rejected. Pricing policies are based upon broad generalizations about the role of arts and culture rather than upon economic realities. Perhaps more important, the role of arts and culture in revitalizing large cities is ignored at all but the most general level. Yet, these large cities must face the stern reality that the economies of agglomeration that attracted manufacturing firms in the past have disappeared for all but a few, specialized industries. The future of the Central Business District may lie not in attracting a few firms to replace the multitude that have left, but in providing recreational and cultural services to residents. In these services, substantial agglomeration economies may yet exist. A cluster of three theaters may be more than three times as attractive as one theater. A cluster of theaters, parks, museums, and art galleries may be even more attractive.

We already observe substantial commitment of private capital directed at the redevelopment of downtown areas in such cities as Pittsburgh, Detroit, and Chicago. Cultural facilities play an important role in all these plans. But how can the chances of success be improved? How can federal support be used most effectively to aid in these local efforts? We cannot answer these crucial questions at this stage. Too little is known about the economic role of arts and culture in the process of urban economic development or, more basically, about many of the factors that affect the demand for arts and cultural activities. This paper is only intended to raise some questions that a broad program of research should be aimed at answering.

II. PURPOSE OF PUBLIC SUPPORT

Public support of the arts is not a new concept. Artists have traditionally been granted stipends or given sinecure positions to allow them to pursue their vocations. Chaucer was appointed to the position of customs officer in the city of London. Spenser wrote "The Faerie Queene" while governing Ireland. Leonardo da Vinci and Michelangelo were proteges of opulent trading families in Florence. Artists were often adornments to royal or rich households. Whether the use of public funds for these purposes reflected public wishes is, of course, doubtful. Not until recently have artists had to consider "earning" their income through the sale of their output, rather than enjoying the more protected environment of a guaranteed income. At the same time, it is only recently that the arts-consuming public has been large enough to support artists on this basis.

Whatever its origins, we are left with a fundamental belief that support of "the arts," however defined, is a responsibility that belongs, at least in part, in the public sector. But exactly what is the role of this government support?

Economists have developed a catalog of cases of the use of public support for an activity in order to encourage increased output, including positive external benefits and income redistribution. These goals and other, less theoretical ones will be explored for the implications they yield concerning how public assistance should be delivered. Some institutional constraints relevant to this issue are also discussed.

Based upon a casual survey of statements by those involved in the arts, there appear to be four broad types of reasons that are most frequently mentioned as justifying public support. These are:

- (1) To allow the economically disadvantaged to purchase admission, by keeping prices low.
- (2) To provide employment opportunities and support for artists.

- (3) To reflect the "option" demand of a large section of the population. While many people may not attend arts events, they nevertheless value the existence of museums, opera, and ballet as a cultural opportunity and they are willing to pay for the continued operation of these activities.
- (4) To provide a focus for the economic and cultural development of both the nation and the local community.

While a number of other reasons might be added, these four categories provide a summary of the separate motivations behind public support. Let us explore each of these in turn.

Reaching the economically disadvantaged. Public support, it is argued, is necessary to reduce ticket prices to a sufficiently low level so that households with relatively low incomes can enjoy cultural activities and facilities. Without support, someone has calculated, museums would have to charge \$10 admission. Some economists have opposed the redistribution of income through the provision of services priced below marginal costs. They have argued that it is better to redistribute income and to allow the recipients to select how they wish to spend their money. This rather simplistic policy ignores a number of sharp political and social realities. First, cash transfers are *politically* difficult to achieve, and recent political developments have not facilitated the process. The prospects for a reform of the welfare system that would increase cash transfers following the demise of the family assistance plan seem slight. The implicit subsidization of low-income groups may be a more palatable approach. A second and related problem stems from the wishes of the donors in any redistribution scheme. Although we may argue that by providing transfers in kind rather than in cash we incur an efficiency loss, the loss may represent a perfectly reasonable price to the donors of purchasing an approved or merit good for the recipients. A taxpayer may be prepared to spend \$10 of his taxes purchasing cultural services for the poor that the recipients value at only \$5, rather than give \$10 in cash that might be spent in any number of less approved ways.

However, although there are convincing arguments for subsidizing cultural services for the poor, there are also convincing arguments against pursuing that policy in the manner in which public support is presently provided. If the poor are to be provided with opportunities for participating in cultural events, then it is the poor who must be subsidized and not the institutions. Free or subsidized admission represents a subsidy to all users, not simply the low-income target households. The facility is denied a large source of revenue from those who would be prepared to pay a reasonable fee to attend, and the effectiveness of public support in reaching target groups is severely diminished. This waste is illustrated in Fig. 1. Let us assume that $D Q_3$ represents the demand for museum attendance and that the museum charges P_1 admission, but would have to raise its prices to P_2 if a public subsidy of S , or $P_2 - P_1$, were withdrawn. The large subsidy of $S \cdot Q_1$ has resulted in only $Q_1 - Q_2$ additional visitors, who, presumably, have relatively low incomes. If the subsidy were withdrawn from the Q_2 people who would attend anyway and devoted to the low-income population groups, then it may be possible to increase attendance to Q_3 , with an increase in revenue to the museum (from $P_2 \cdot Q_1$ to $P_2 \cdot Q_3$). While the NEA has often argued that it wishes to use its funds to mobilize private donations, it has paid much less attention to the problem of mobilizing funds from audiences.

There are a limited number of experiments under way to ascertain the effectiveness of the allocation of cultural ticket vouchers to low-income households.¹ The future success of the NEA and of state and local cultural and recreational agencies lies in a movement away from institutional subsidies toward audience subsidies. There would be two important indirect benefits of a program aimed at reaching out to such population groups. First, cultural facilities would become more responsive to the needs of the central city population they should serve. In order to attract audiences (and to collect the voucher subsidies) they would be encouraged to work with local boards of education and

¹Cut price vouchers are made available to low-income households through welfare offices and local human resource agencies. The museum or theater is able to redeem these vouchers for cash from the sponsoring authority.

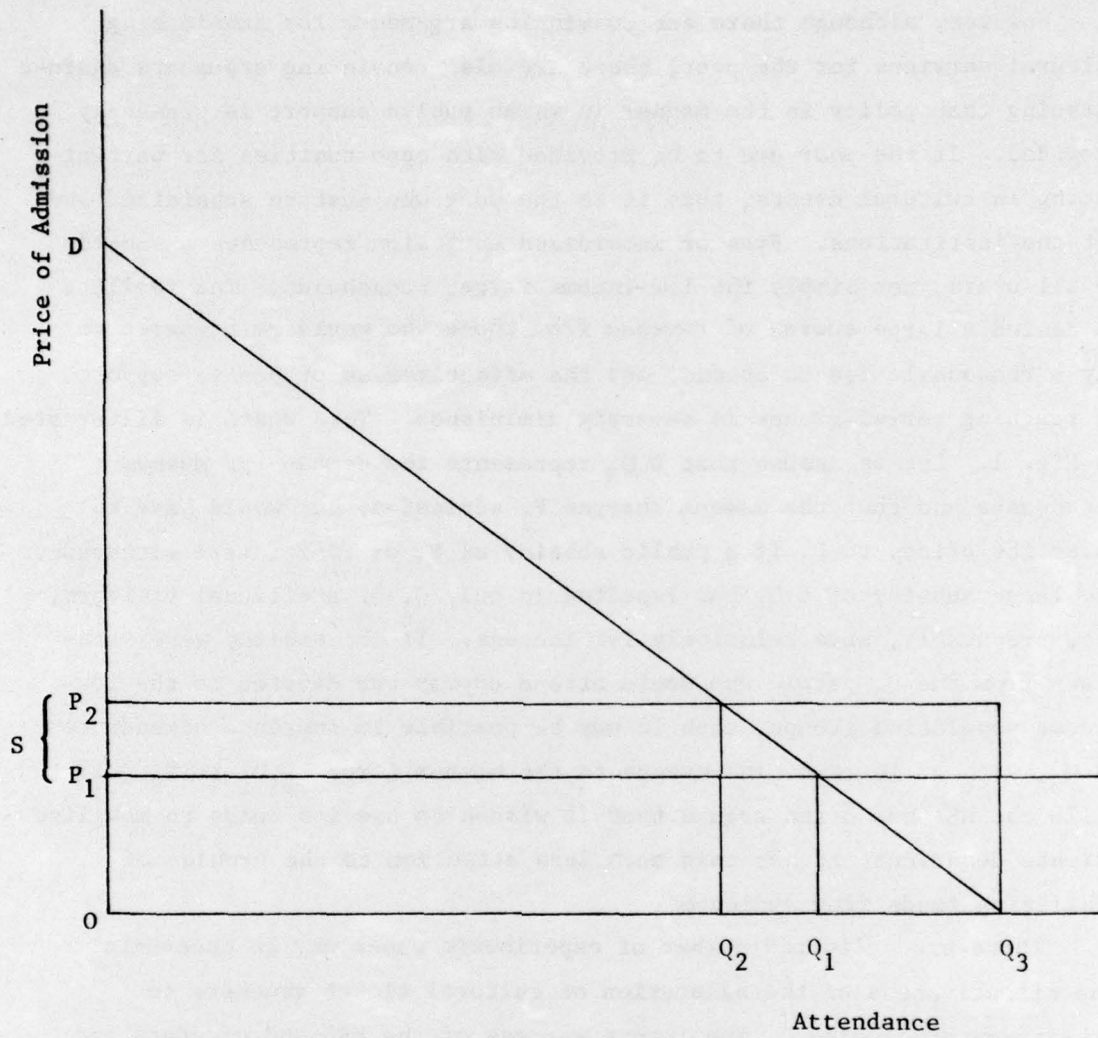


Fig. 1--Museum Attendance and Pricing

local public service offices. Second, increased participation by the economically disenfranchised might lead to perceptible reductions in crime and vandalism, symptoms of the urban frustration of low-income groups. We should not forget that the National Advisory Committee on Civil Disorders (1964) found that inadequate recreational facilities ranked fifth (immediately after the neglect of education) among reasons for discontent among urban blacks.

Employing artists and performers. The NEA has frequently argued that public support is necessary to provide employment opportunities for artists. The usefulness of projects conducted during the depression with WPA funds in which artists and poets were employed is cited as a precedent. The precedent is misleading. The NEA provides continued support for the arts, not simply countercyclical support. If the goal were to provide income for artists, then support would be given directly to the artist rather than to institutions. Although the NEA does provide some direct support, most of its resources are devoted toward institutions. The extent to which such support is translated into higher incomes for artists is uncertain.

Some proponents of support for the arts have argued that it is necessary to support an artist during his or her lean years in order that he or she can develop into an artist of stature later on. However, art galleries and publishers have shown a remarkable talent for performing this function. The pecuniary rewards for success in the arts are considerable and, although the imperfections of the capitalist market in allowing for the development of human skills and knowledge are well-known, this function may not be one in which public agencies have a comparative advantage. It should be noted that subsidies to selected audiences would also provide for the employment of artists.

Option demand. Since Musgrave identified this concept, it has been liberally applied in the recreational and cultural field. It is argued that many people demand the option to attend recreational and cultural events even if they do not actually attend them. The knowledge that the opportunity is there is a service for which consumers would willingly pay.

Obviously, the market is an inadequate mechanism through which this demand can be expressed and supplied. However, it is not completely inadequate. Many cultural institutions sell "memberships"--museums, public television, and repertory theater are examples--which may not actually sell services, but offer the right to be first to purchase tickets to performances, or serve as badges of "friendship." This enables those with strong option demands to express them and the relevant facilities to collect the revenue. For many people, however, the option demand may be relatively weak, perhaps a few cents a year, and the costs of collecting from these people--advertising, direct mailing, and administration--make it uneconomic to collect any revenue from this demand. In this case, federal and local tax collection and redistribution may be a much more effective method.

Although it is a popular argument, the exact nature of option demand remains elusive. It is not the latent demand of a group of the population that will be exercised sometime in the future. This demand can be met if and when it is expressed by increasing the supply of cultural facilities and activities. The rapid expansion of dance companies in the last ten years attests to the responsiveness of supply to increases in demand. Neither can the case be made that the "death" of an institution represents an irreplaceable loss of the sort that would result from damming the Colorado River to fill the Grand Canyon. The dissolution of a dance company still leaves dancers, choreographers, and composers intact. The dissolution of a museum still leaves the works of art intact.¹ Option demand is more abstract than either of these issues. Option demand is probably expressed for other activities that do not benefit from public support. For example, members of a local community who do not attend ballgames value their local ball club, and might be prepared to pay to support their local club. To some extent, we can trace the ability of the arts to gain public support to the political influence of the patrons of the arts. The role of the arts in meeting other social objectives,

¹ Although some of the artworks could disappear from view into private collections.

although often asserted, remains unclear.¹ We cannot conclude, from the assertion that there is an option demand for cultural activities, what type of support the arts should be given. Is the option demand for facilities at a particular location or for particular performers? Further research, using subscription data and other sources of information, as well as some basic theoretical work, should be directed toward a deeper understanding of this concept, its determinants, and its implications for public policy.

The arts as an economic growth pole. Many local government officials regard cultural facilities and activities as a *growth pole*--a civic attraction that will draw tourists and suburban residents, and will provide a basis for economic growth and development. Orchestras are used to provide lunchtime attractions for shoppers, urban renewal efforts grow up around theaters, and local parks are decorated with community murals.² Studies have been commissioned that show the high rate of return that local governments earn from investment in the arts. Unfortunately, the evidence in this area is meager. Anyone who has worked with employment data by Standard Industrial Classification (SIC) code is aware of the difficulties of trying to measure the employment effects of an activity as ill-defined as "the arts." The motivation of stimulating economic and social development through public investment in the arts perhaps explains the present financing methods better than the three previous goals. The arts might be regarded as an activity analogous to basic research. Institutions are funded because they are unable to appropriate the full benefits resulting from the

¹ Senator Jacob Javits, in a speech commemorating the tenth anniversary of the founding of the NEA (he was one of the co-sponsors of the original bill that set up the organization), claimed that through the arts, all our social ills could be cured. Others have made less extravagant but similar claims.

² Detroit's massive redevelopment plans prominently feature theaters and concert halls. At a different level, the new zoning ordinances introduced in New York City in the 1960s offered height incentives to developers who included theaters or open space in the plans for their office developments--an incentive, incidentally, which over 90 percent of the developers chose to accept.

services they provide. Because of the unpredictable nature of the outcomes of artistic endeavors, or of basic research, funding is directed toward institutions rather than toward individuals or specific projects. The selection criteria are based upon the probability of some form of success--the past performance, the proven or potential skill of those within the institutions, and the judgment of the sponsors. Public support of the arts is therefore an investment in basic research, whose development will lead to the development of future institutions and to the growth of support activities--restaurants, night clubs, art galleries, and service industries. These activities will provide employment opportunities for local residents and tax revenues for the city.

If the NEA is to act in a similar role to the much larger National Science Foundation, it must undertake a much more careful look at the process of fund allocation. Much less is known about the secondary developments that may result from the investment in cultural institutions than is known about the research and development process in the physical sciences. Although the NEA has recently undertaken to sponsor research into the measurement of the economic impacts of cultural activities, the effort is too small to provide the information necessary for an effective evaluation of those impacts. Further research is urgently needed in this area.

While it does indeed appear, from its history of financing cultural institutions rather than audiences or artists, that the NEA sees the role of public support of the arts as providing basic research "seed" money, mention should be made of an institutional factor that also tends to support institutions rather than other players in the cultural area. The income tax structure has created an incentive for donors to give to non-profit corporations. Tax "breaks" are not forthcoming to those who give to individuals rather than to designated organizations. Donations to audiences are likewise penalized. Because of the perceived complementarity between private and public contributions, the NEA has followed the private sector in the disbursement of its funds.

III. CONCLUSIONS

Four major goals of public policy in supporting the arts have been reviewed. Only one of these goals--the use of cultural facilities as a growth pole, or focus--clearly explains why public money should be given to institutions rather than to audiences or to artists themselves. However, the other goals frequently have been expressed as desired policy outcomes. In view of this, we can make two major policy recommendations.

First, a much greater effort should be devoted toward the direct subsidy of audiences rather than institutions. Research should be undertaken to determine what factors affect the demand for cultural activities by selected population groups and what are the outcomes, both social and economic, of increased participation by these groups. Cooperation between federal and local agencies should ensure that these subsidies have the greatest possible desired effect.

Second, the role of cultural and recreational facilities in the economy must be examined in much greater detail. What kind of facilities enjoy the most powerful economies of agglomeration? How should services be priced? Which facilities and activities should be provided by the public sector and which would be provided by private resources responding to demand?

These are a broad and complex set of questions. By clarifying the policy perspective, it is hoped that a contribution has been made toward the basic problem of asking the right questions. It is up to those engaged in research in these areas to provide the answers, and to those with the public money to provide the necessary resources.